MINUTES
of the
FIRST MEETING
of the
REVENUE STABILIZATION AND TAX POLICY COMMITTEE

June 5, 2008
Room 322, State Capitol
Santa Fe

The first meeting of the Revenue Stabilization and Tax Policy Committee was called to order by Representative Edward C. Sandoval, chair, at 9:15 a.m. in Room 322 of the State Capitol in Santa Fe.

Present
Rep. Edward C. Sandoval, Chair
Sen. Carlos R. Cisneros, Vice Chair
Sen. Mark Boitano
Rep. Anna M. Crook
Sen. Dianna J. Duran
Rep. Keith J. Gardner
Rep. Roberto "Bobby" J. Gonzales
Sen. Timothy Z. Jennings
Rep. Ben Lujan, Speaker of the House
Sen. Bernadette M. Sanchez
Sen. John Arthur Smith

Absent
Sen. Kent L. Cravens
Rep. William J. Gray
Rep. George J. Hanosh
Rep. Daniel P. Silva
Sen. H. Diane Snyder
Sen. James G. Taylor
Rep. Thomas C. Taylor

Advisory Members
Rep. Janice E. Arnold-Jones
Sen. Sue Wilson Beffort
Sen. Phil A. Griego*
Sen. John C. Ryan
Rep. Henry Kiki Saavedra
Rep. Donald E. Bratton
Rep. Nathan P. Cote
Sen. John T.L. Grubesic
Sen. Gay G. Kernan
Sen. Cisco McSorley
Sen. Steven P. Neville
Rep. Andy Nuñez
Rep. John Pena
Sen. Leonard Lee Rawson
Rep. Debbie A. Rodella
Sen. Nancy Rodriguez
Sen. William E. Sharer
Rep. Don L. Tripp
Rep. Luciano "Lucky" Varela

* Permission to attend granted

Staff
Pam Ray
Tim Crawford
Doris Faust
Cleo Griffith
Doug Williams

Guests

The guest list is in the meeting file.

Copies of all handouts and written testimony are in the meeting file.

Thursday, June 5

Interim Committee Protocol

Paula Tackett, director, Legislative Council Service (LCS), presented basic protocol for interim committees. She discussed quorums and the ways in which, and purposes for which, quorums are counted, voting privileges, taking official committee action with or without quorums and the ability of a single house to block adoption of committee motions. She reminded members that a majority of committee members of both houses must vote for a proposal or it will fail. Failure of a proposal to obtain a majority of votes of the committee members of either house will "block" the proposal from approval. The number of positive votes from each house must equal at least a majority of the committee members appointed to the committee. This means that if there are no members, or fewer than a majority of the committee members, from one house present, no official action may be taken by the committee unless the action is taken by consensus or without objection and no one challenges the quorum.

She also reminded members that they should close their laptops when speaking into the microphones because the microphones are voice-activated and require a direct line of sound without impediment to operate correctly.

Introductions

The chair asked that committee members introduce themselves and that staff be introduced by Ms. Ray, staff attorney, LCS.

Post-Session Fiscal Update

David Abbey, director, Legislative Finance Committee (LFC), and Norton Francis, chief economist, LFC, presented the post-session fiscal update.

Mr. Abbey spoke about the efficiency with which House Bill 2 was presented to the governor and signed during the 2008 legislative session. The general fund budget revenues enacted for FY09 were $6.035 billion. This is a 6.3 percent increase over the FY08 general fund operating budget expenditures. He noted that the change to accrual accounting was still presenting occasional issues with the budget. For FY09, the general fund budget expenditure growth declined as a share of New Mexico personal income to under eight percent, the lowest expenditure rate of expenditure growth as a percent of personal income in a decade.

General fund reserves remain strong at 10.3 percent of recurring general fund appropriations for FY09. This high level of reserves reflects the concern of both the legislature and the executive regarding the volatility of the energy revenues and a slowing economy.

The economy, Mr. Abbey noted, has taken a dramatic downward turn since the consensus revenue estimate in December 2007. Many national economists have concluded that the country is in a recession, although Global Insight, one of the economic forecasting groups relied on by the state, believes that if the nation is in a recession, it will be short and shallow, with growth returning to three percent in FY10.

Nonrecurring general fund revenues in the General Appropriation Act of 2008 totals approximately $147.6 million. Senate Bill 471 (Chapter 92) appropriates $123 million of the general fund revenue for capital outlay projects. Reserves are approximately $623.5 million, or 10.3 percent.

Of new recurring funds, public schools absorb the greatest percent, at 43.3 percent. New Medicaid funding totals 23 percent of the new recurring funds available.

Prison population is decreasing as Clayton will see its new corrections facility opening. The system has 600 unfilled beds currently, and the new capacity will be difficult to fill. Although the legislature appropriated an additional $4 million to reduce the waiting list for the developmentally disabled, Mr. Abbey projected it will take 25 years at that rate to eliminate the waiting list.

Mr. Francis gave an economic update. Although the revenues from oil and gas are projected to increase, gross receipts taxes from general sales, selective excise taxes, corporate income taxes, license fees, rents and royalties and other miscellaneous receipts are showing decreases. Energy revenue will continue to offset the decreases in these broad-based taxes that rise and fall with the economy. The high fuel prices have no effect on revenue from the fuel taxes except that, at some point as the price inflates, the volume of fuel sold will decrease. Fuel taxes are based on volume distributed and are not a percent of the price. He noted that employment has fallen below two percent growth to a low of less than one percent growth in May 2008. Personal income is falling and was lower in May 2008 than in November 2007. The next consensus group revenue estimates will be presented at the August meeting in Ruidoso.

Committee discussion included concerns about substantial losses that have been experienced by investments of the State Investment Council, the Educational Retirement Board, the Public Employees Retirement Association and the Retiree Health Care Authority. Gaming revenues for FY07 did not increase at the rate anticipated, and there has been no decrease in lottery revenue.

Introduction to Yield Control

Tom Clifford, research director, New Mexico Tax Research Institute, and Al Maury, Chief economist, Taxation and Revenue Department (TRD), together presented to the committee a basic introduction to yield control.

Mr. Clifford began with general facts about property taxes. He discussed recent trends in tax values and obligations, the tax policy criteria relevant to evaluating property taxes and current policy issues with the property tax in New Mexico. A handout is in the committee file.

Property tax generates about $1.3 billion in revenue annually. The taxable property base is approximately $47 billion. Taxable value is one-third of the valuation of a property less the exemptions that may be applied to the value. Fifty-six percent of the tax base is residential property, 30 percent is nonresidential property and 14 percent is oil and gas or copper mineral property. Property tax rates, assessed in mills (one dollar per $1,000 of taxable value), are not uniform throughout the state and vary from a low of 10 mills to a high of 45 mills. The average mill levy in New Mexico is around 27 mills, or about 0.9 percent of market value. Approximately one-third of property tax revenue goes to the public schools, generally for capital outlay purposes. One-fourth of the property tax revenue goes to counties for operating expenditures. One-sixth goes to municipalities, mainly for operating expenditures. The University of New Mexico Hospital, other hospitals and higher education receive about one-tenth of the property tax revenue. General obligation bond issues are repaid with slightly less than one-twentieth of the property tax revenue.

In the 10 years from 1998 to 2007, net taxable values for residential property more than doubled, increasing by 105 percent. The next taxable value of oil and gas property increased by 142 percent. Nonresidential property net taxable values increased by 61 percent. Tax obligations increased 98 percent over that 10-year period, oil and gas taxes increased 162 percent, residential obligations increased 112 percent and nonresidential obligations increased by 65 percent. Tax rates have remained fairly constant over this 10-year period: residential rates increased from 25.9 mills to 26.7 mills; nonresidential rates increased from 28.5 mills to 29.1 mills; and the largest increase of rates in the 10-year period was in oil and gas rates, where the increase was from 20.7 mills to 22.4 mills. On average, these figures indicate that yield control is working fairly well, even with the increased debt and other distortions that are included in determining rates.

Mr. Clifford concluded that residential property values have not kept pace with house price inflation. The three-percent limit on residential property valuations has caused a wedge to develop between properties that are newly purchased and properties that have been held for a long period of time. Valuations for residential property held for longer periods of time are lower than house price inflation. If the value of residential property increases at a slower rate than the inflation factor due to the inclusion of the value maintenance factor that incorporates values held to the three-percent increase limit annually, then the rate of property taxes will increase to cover the needed revenue to keep the revenue at a stable level.

Mr. Maury discussed the way yield control was developed and how it is applied to values. Before 1979, when yield control was first adopted, assessors were hesitant to raise valuations of property to current and correct values because the increase in valuations would cause an increase in the tax assessment. Yield control was designed to ***decrease*** property tax ***rates*** as ***values increased****,* or vice versa, so that there would not be a windfall to the taxing district because values were simply brought into line with the real-world market by being raised to current and correct values. The theory is that as values increase, rates can decrease to generate a targeted amount of revenue. If values fall, the rates would rise so that district operating funds do not fall short of needs. Not all components of a tax rate are subject to yield control, and factors that distort or depress property values from current and correct values or affect rates without yield control being applied lessen the ability of yield control to reduce rates and maintain slowed growth in rates. Mr. Maury noted that yield control is a formula for restricting revenue yields by changing rates in response to reassessment or valuation maintenance. Revenue yields tend to increase when yield control is applied to values that reflect the rate of inflation in the absence of reassessment, so that when reassessment occurs, the rates have changed over time to approach the new levels.

The yield control formula has the following three significant variables that result in the mill rate to be levied to provide operational revenue: 1) valuation maintenance, which includes changes in assessed value of existing properties due to reassessment; 2) a government cost index that reflects the rate of inflation in the housing market; and 3) new construction, also called net new value.

As the government cost index increases, rates will increase by the same percent up to five percent if all other variables are kept constant. Values of new construction or net new value do not change the resulting rate significantly, but increase the base values in direct proportion to the increase in net new value or new construction; a four-percent increase in new construction would produce a four-percent increase in the previous year's base and also a revenue increase of approximately four-percent. Valuation maintenance is inversely proportional to the percent of the prior year's base that is valuation maintenance for this year, so if homes are reassessed and increase in value by seven percent, that factor will appear in the denominator of the formula and will cause a decrease in rates by dividing other factors by 1/1.07, or 0.93 percent.

In summary:

- yield control has operated to hold down operational mill levies in most counties on rates subject to yield control;

- the impact of yield control has been greater on residential tax obligations than on nonresidential tax obligations;

- lack of data prevents knowledge of exactly how yield control is affected by the three percent valuation limitation; in general, it can be said that yield control would tend to mitigate the increases in revenue that would be seen due to reassessment of property at the time it is transferred, although yield control would have no effect on individual property tax valuation increases due to transfer and reassessment. Yield control would have an effect on the mill rate once all valuations are considered and would tend to keep the operational mill rate lower as property values increased due to reassessment or rose with the increase in value of up to three percent per year on property not transferred; and

- yield control does not apply to debt service rates.

Committee Work Plan, Schedule and Budget

Ms. Ray presented the proposed work plan, schedule and budget to the committee. Discussion ensued regarding the items on the work plan.) Several more were added at the request of committee members. (See the attached proposed work plan). An additional day was included for the Farmington meeting to accommodate the tours of the BHP long wall underground coal mine and the PNM electric generating plant. All other tours will be incorporated into the meetings, possibly by scheduling them in the afternoon prior to the first day of the meeting. Added items were:

- to review the number and purpose of quasi-governmental entities that have been authorized to levy taxes and determine the rate, amount and type of taxes imposed and whether those authorities are or should be subject to yield control;

- to review regulatory reform and review Senate Memorial 53 on administrative process and regulatory reform;

- to review special methods of evaluating property taxes for various industries, such as power plants or railroads;

- to include in the tax increment development district (TIDD) discussion an examination of the effect of including existing businesses in TIDDs; and

- to examine possibilities for broadening county and municipal tax bases to increase revenues without putting additional burdens on existing taxpayers and review the changing needs of communities due to additional federal mandates.

The committee chose to have its August meeting in Ruidoso. The committee also asked that money be included in the budget for expert testimony on TIDDs and combined reporting of corporate income tax. Ten thousand dollars will be added to the budget for expert testimony.

2008 and Recently Implemented Legislation

Rick Homans, secretary of taxation and revenue, and Jim Nunns, tax policy director, TRD, presented information about the taxation and motor vehicle bills that were adopted in the 2008 legislative session. Also discussed was legislation adopted in previous sessions that is now beginning to be implemented.

The bills adopted in the 2008 legislative session are listed below.

- House Bill 324 contains the charitable care property tax valuation changes. This bill provides an exemption from valuation for property taxation purposes for property operated as a community to which the Continuing Care Act applies, or operated under the regulatory control of the Department of Health. This change will be applicable in the tax year that began January 1, 2008.

- Locomotive fuel tax is exempt from gross receipts and compensating tax beginning on July 1, 2009 if construction on a locomotive refueling facility has begun and is certified by the Economic Development Department, or on July 1, 2010 if the Economic Development Department does not certify that the construction has begun until January 1, 2010.

- House Bill 615 amends the process for distributing county gross receipts tax revenue pursuant to Section 7-1-6.13 NMSA 1978. An additional distribution from revenue is attributable to the second one-eighth increment of the county gross receipts tax imposed by a county to the Sole Community Provider Fund. The new distribution each month is equal to one-twelfth of the amount of the county's approved contribution for support of the sole community provider payments. The provisions became effective on February 28, 2008.

- House Bill 661 amends Subsection B of Section 7-36-15 NMSA 1978 that requires valuation authorities (the TRD or county assessors) to apply generally accepted appraisal techniques when appraising property for property tax purposes. When appraising residential housing, the valuation authority must take into consideration any decrease in value that would be realized by the owner in a federal, state or local affordable housing program.

- Senate Bill 174 extends the time in which the high-wage jobs tax credit may be claimed until July 1, 2015. The Economic Development Department must report to an appropriate interim legislative committee.

- Senate Bill 574 permits the TRD to rectify a problem that exists because the TRD erroneously collected income tax from the military service pay of Native Americans who were domiciled on New Mexico Indian reservations during a period of service in the military. A study will be conducted by the secretary of veterans' services to determine which veterans were affected. The study will identify the survivors of deceased veterans who had taxes erroneously withheld. The secretary of veterans' services will set up the process to return funds overpaid to the taxpayer. Senate Bill 574 went into effect on March 4, 2008.

- Senate Bill 438 puts into effect new weight-distance penalty assessments and a graduated scale of penalties for subsequent offenses. This bill became effective on May 14, 2008.

- House Bill 218 made some corrections to the small counties assistance formula to amend the inflation factor so that it tracks changes better. This bill becomes effective on July 1, 2008.

- Senate Bill 43 increases the maximum production that a winery can have and still be considered a "small winegrower" to 950,000 liters. The liquor excise tax of $.20 per liter is extended to those small winegrowers producing up to 950,000 liters of wine. The law clarifies the status of wine transferred between wineries for various purposes. These provisions become effective on July 1, 2008.

Motor vehicle legislation also was adopted during the 2008 session. The following describe those bills.

- House Bill 100 provides penalties for tampering with ignition interlock devices. These changes became effective on February 29, 2008.

- Several specialty license plates were adopted during the 2008 legislative session. They include license plates for the City of Las Cruces and breast cancer awareness and specially designed plates for Purple Heart recipients.

- House Bill 215 eliminated waivers for testing for commercial driver's licenses and also removed a subsection from Section 66-8-102 NMSA 1978 that appeared in the law due to adoption of two amendments to that section in 2007. The last bill amending that section was compiled, but it showed the subsection, even though the subsection had been removed by the bill amending the section that was signed first. It was confusing, and the federal government was concerned that the definition of "conviction" in the subsection would still be valid, or at least cause confusion. It was basic cleanup that normally would have occurred in the normal course of amending the section in the future, but was included in House Bill 215 to remove the confusion as quickly as possible. This bill became law on May 14, 2008.

- Senate Bill 551 provides for multiple-trip special permits for agricultural product transport vehicles to allow those vehicles to pass through ports of entry without stopping on each trip, provided that the transported agricultural products were harvested in New Mexico or in a state adjacent to New Mexico. This bill became effective on May 14, 2008.

Other bills became effective after 2008.

- Senate Bill 116 changes the eligibility requirements for limitations on increases in assessed value of property owned by low-income taxpayers who are 65 years of age or older or are disabled. This provision now extends the upper limit of income eligibility to incomes of $32,000 or less. This will be applicable to property tax years beginning on or after January 1, 2009.

- Senate Bill 164 provides for a distribution from liquor excise tax receipts to Farmington in San Juan County for programs for street inebriates. The distribution should amount to $20,750 per month. This provision becomes effective on July 1, 2009.

- Senate Bill 177 provides an option to taxpayers to prepay property taxes in 10 monthly installments beginning on June 1 of a tax year and ending on March 1 of the following year. Each monthly payment shall be 10 percent of the tax due to the state based on the prior year's property tax bill, and the last payment shall include the balance due for the year. This provision becomes effective on January 1, 2009.

The general fund revenue impacts of the legislation enacted in 2008 are all positive, but small. The largest impact, occurring in FY10 and totaling $6 million, is from the effect of the locomotive fuels tax.

Bills adopted in prior years but becoming effective in 2008 are listed below.

- Reduction in the income tax rate to 4.9 percent, the final year of the governor's income tax rate reductions adopted in 2003.

- House Bill 436 from 2007 became effective on January 1, 2008. It amends the penalty and interest provisions of the Tax Administration Act, increasing the minimum penalty for unpaid taxes to $25.00 from $10.00, but lowers the interest paid on under- or over-payment of taxes. The maximum penalty for failure to pay a tax or to file a return due to negligence or disregard of TRD rules is increased to 20 percent of the tax due. Other administrative requirements are also included in the bill.

- Senate Bill 463 from 2007 amends the renewable energy production tax credit to allow it to be claimed only by facilities that first produce electricity before January 1, 2018. The law also changes the rate of the credit applied and decreases the credit for the taxpayer beginning in the seventh year of production. The size of the facility that may claim the credit is reduced to facilities producing one megawatt. The maximum amount of electricity that may be certified as eligible for the credit is increased for solar facilities only by an additional 500,000 megawatt hours of solar-generated power. A total of 2.5 million megawatt hours from all power sources can be approved for credits, with the last 500,000 megawatt hours at least being produced from solar energy. This law also became effective on January 1, 2008.

- Senate Bill 463 from 2007 creates corporate or individual income tax credits for agricultural water conservation expenses and sets a sunset date of January 1, 2013.

- Senate Bill 340 from 2007 specifies how properties associated with oil and natural gas transmission are to be assessed for property tax purposes. The law also specifies that a claim of reduced value by the taxpayer due to economic or functional obsolescence must contain an obsolescence factor and a brief statement of facts supporting the claim.

The TRD also described several other bills that became effective in 2008 that create specialty license plates, and House Bill 1283 establishes a fund that drivers may contribute to at the time of registration that will be used to help save children's eyesight.

The last three items that the TRD discussed were gross receipts tax districts that were created in 2008: Mesa Del Sol created its TIDD; SunCal New Mexico created its Upper Petroglyph TIDD; and the regional spaceport district was created in Dona Ana and Sierra counties. Three water and sanitation districts were created: El Prado Water and Sanitation District in Taos County; El Valle de Los Ranchos Water and Sanitation District in Taos County; and Valley Water and Sanitation District in San Juan County.

It was noted to Kenneth Ortiz, director, Motor Vehicle Division, TRD, that since the registration stickers are no longer color-coded by year of expiration, it is more difficult for law enforcement to determine if a car is properly registered with a cursory glance at the license plate.

Mr. Nunns noted that as special districts levy taxes, they report their progress to the TRD.

Bernalillo County Property Rate Composition

Karen Montoya, Bernalillo County assessor and vice chair of the Assessors Affiliate of the Association of Counties, began the discussion of how property rates are determined by describing how she values property in Bernalillo County. She discussed the complexity of determining the values without the ability to use sales affidavits. The computer-assisted mass appraisal (CAMA) system, a computer software system that helps determine property values, is instrumental in facilitating the valuation process. First, she collects data on parcels in Bernalillo County and identifies the new construction. This data is entered into the CAMA system. Cost tables are created and then use sales affidavit information from residential properties and market trends to adjust the cost tables as needed. The parcel data are used to create an appraised value that represents the market value of the property. She provided the committee with several sections of the Property Tax Code to illustrate her duties. Section 7-36-16 NMSA 1978 deals with responsibilities of county assessors and defines "current and correct" values of property. Section 7-36-21.2 NMSA 1978 discusses limitations on increases in valuation of residential property, providing for the three-percent limit on valuation increases if a residential property is not transferred. She noted that Bernalillo County uses a computer program to review all of the values assigned to residential property to ensure that the increases each year do not exceed the permitted three percent.

Rick Silva, director, Property Tax Division (PTD), TRD, and Mitch Bonney, bureau chief, State Assessed Bureau, PTD, TRD, presented the steps that are taken by the TRD to review the valuations provided by each county assessor. The TRD mainly checks to make certain that none of the values appears to be out of line with the prior-year values. County assessors have a one-month period in which to certify the values from all of the counties. They also must certify the values presented for higher education, public school districts and other special districts with taxing authority.

Robert Apodaca, director, Local Government Division (LGD), Department of Finance and Administration (DFA); John Gallegos, bureau chief, Budget and Finance Bureau (BFB), LGD, DFA; and Isaac Montoya, executive analyst, BFB, LGD, DFA, described in detail how they apply the yield control formula to the certified values they are given by the TRD. They noted that, previously, there was only one staff person who performed the yield control calculations, but thanks to improved budgets, there are six who deal with yield control. In addition, computers have made the job more possible. Mr. Montoya noted that many assessors are still not using computer technology to develop their valuation data, and this causes slow turnaround and inaccuracies. The Department of Information Technology (DOIT) tends to view assessors as revenue generators and not data processing agents. The DOIT has not worked to make the assessors' computers compatible with the TRD or to ensure that all assessors have adequate information technology to complete their valuations accurately. Now, yield control is not the only factor in setting property tax rates. Other factors, such as debt service and special districts that are not subject to yield control, also are added to the yield-controlled millage to create the total millage.

Patrick Padilla, treasurer, Bernalillo County, distributed a sample tax bill sent out by his office. He provided the committee with copies of Section 7-38-37 NMSA 1978, which describe the contents of a property tax bill. Section 7-38-38.3 NMSA 1978, which allows for property taxes to be paid in 10 monthly installments, was also included with Mr. Padilla's handouts.

The committee adjourned at 3:15 p.m.